

BAKER & McKENZIE

RESPONSE TO CONSULTATION ON THE NON-HORIZONTAL MERGER GUIDELINES

Baker & McKenzie welcomes the opportunity to comment on the draft Notice. In general, we think it helpful to have guidance of these types of mergers. We also note the Commission's efforts to align its approach with that taken in the Notice on Horizontal Mergers.

1. DEFINITIONS/KEY CONCEPTS

- 1.1 In paragraph 10, the Commission explains that merger control enables it to intervene when a merger significantly increases the market power of firms. We suggest adding "to the extent that the merger significantly impedes effective competition" after "market power of firms" (since this is the pre-requisite for intervention by the Commission).
- 1.2 We welcome paragraph 11 (which acknowledges, to a degree, that non-horizontal mergers raise less issues than horizontal mergers). However, we consider that paragraph 11 understates the unproblematic nature of the vast majority of these mergers. In our view the word "generally" should be deleted and replaced with "very much". This is necessary since it is crucial for the guidance to express the correct level of likely concern in order to avoid them having a chilling effect on these mostly pro-competitive mergers. Overall, if the guidelines are to be of help rather than a hindrance to companies and national authorities looking for guidance on specific cases, it is vital that the guidance should not raise purely hypothetical problems which are extremely unlikely to arise in practice as if they are real risks which need to be examined in detail in all cases.
- 1.3 In our view, the introductory statement in paragraphs 11 and 12 should also make it clear that the Commission (and thus NCAs which will no doubt rely heavily on this Notice) will need to ensure that any intervention is based on high quality evidence. This is necessary since - as the ECJ warned in *Commission v Tetra Laval BV*¹ - the Commission must undertake a prospective analysis in which "the chains of cause and effect are dimly discernible, uncertain and difficult to establish".
- 1.4 Paragraph 18 of the draft Notice defines "anticompetitive foreclosure" as arising when companies "may" be able to profitably increase prices for consumers. In our view, the draft Notice should provide more certainty by explaining that anticompetitive foreclosure only arises when a company "would" be able to profitably raise prices - otherwise the anticompetitive foreclosure could be said to have arisen despite the existence of counter-strategies, likelihood of re-entry etc. Further, the concept of "increasing prices" in footnote 8 already includes a speculative component since it covers the situation where a price "may" be more likely to increase than it would have been without the merger.

2. VERTICAL MERGERS

Market share and concentration levels

- 2.1 *Paragraph 25 (opening text):* We agree that it is more appropriate to specify a threshold beyond which there *may* be competition issues - as opposed to specifying a threshold beyond which issues will be deemed to arise. However, in our view, a 40% threshold is appropriate since this reflects the dominance-based test for mergers (as opposed to 30% which is more appropriate when applying the stricter test which applies to restrictive agreements). In addition, we query why the safe harbour is only available when the market share is below [40] % in both markets. It seems to us that there would only be competition issues if there was at

¹ Case C-12/03 P, *Commission v Tetra Laval BV*, ECR 1000, paragraph 44.

least some significant share in both the upstream and downstream market. We therefore suggest that "in each of the markets concerned" (paragraph 25, 3rd line) be replaced by "in either of the markets at the upstream and downstream levels concerned". We also believe that an HHI of below 2000 is too low - since this reflects only a moderate degree of concentration and so is more appropriate as a safe harbour for horizontal mergers.

- 2.2 *Paragraph 25(a)*: In the interests of clarity, the Commission should define what it considers to be "in the near future" (in the same way that the guidelines on vertical agreements clarify that a potential competitor is a company that would be able to enter the market within one year).
- 2.3 *Paragraph 25(b)*: The Commission should also clarify what is meant by a "significant" cross-shareholding - e.g. a shareholding of 15% or more?
- 2.4 Paragraph 26 (4th line): This line should refer to "dominance" and not the lower level of "market power".
- 2.5 *Paragraph 56*: We suggest that "(if these are practically feasible alternatives)" should be inserted after "vertical agreements".
- 2.6 Paragraph 58: This paragraph refers to whether the merged entity would have the incentive to reduce its purchases upstream without adding "'so as to foreclose rivals' access'" which we suggest be added at the end of line 4 to take account of the fact that purchasing patterns may simply be realigned by the merger (as is accepted in paragraph 36 in respect of input foreclosure risks).

Vertical mergers - customer foreclosure

- 2.7 *Paragraphs 67-70*: This section of the Notice should acknowledge that, in certain markets, it would not make commercial sense for a vertically integrated company to eliminate purchases from an upstream rival - e.g. in certain retail markets where a multi-brand offering is needed in order to be a viable player on the downstream market.
- 2.8 *Paragraphs 71-76*: The first sentence of paragraph 73 suggests that a vertical merger may give rise to a SIEC in the upstream market (when a sufficiently large fraction of upstream output is affected by the revenue decreases resulting from the vertical merger). This appears to contradict paragraph 16 of the draft Notice which emphasises that the Commission is concerned about anticompetitive effects at the downstream, consumer facing level of the market. The Commission should therefore clarify that, although foreclosure may arise upstream, intervention is only appropriate when that foreclosure translates into anticompetitive downstream effects.
- 2.9 *Paragraph 77*: The Commission explains that, by becoming the supplier of a downstream competitor (and thereby becoming privy to confidential information), the merged entity may put that competitor at a competitive disadvantage. However it seems to us that some analysis of market power is required here since, absent market power at the upstream level, the 'disadvantaged' downstream rival could simply switch to another supplier.
- 2.10 *Paragraphs 78-89 (on coordinated effects)*: The draft Notice only refers to certain parts of the section in the Notice on Horizontal Mergers on coordinated effects. It is unclear whether advisers should infer from this omission that other parts of that section do not apply. Overall, it is our view is that paragraphs 78-79 risk being overly broad - particularly when compared to the corresponding sections on foreclosure. More specifically:
- Unlike the corresponding section in the Notice on Horizontal Mergers, the draft Notice does not point out that it is easier to co-ordinate on a price for a single homogeneous

product, rather than in the context of a market with many differentiated products (or where demand and supply conditions are unstable).

- Query whether it is always the case that vertical foreclosure will make coordination among the remaining players easier. In fact, it will not necessarily increase symmetry between them but may actually reduce such symmetry as already exists prior to the merger. For example, if a vertically integrated entity elected not to sell an important input to a particular customer downstream, it does not follow automatically that there is greater scope for the merged entity and other upstream suppliers to coordinate. In an oligopolistic market, it is conceivable that there would be a reduction in competitive pressure upstream, but this is an example of non-coordinated effects and is already dealt with in paragraph 37.
- The proposition that foreclosure facilitates co-ordination is simplistic and overlooks the fact that the vertical integration may give rise to less symmetrical market structures (and therefore a lower likelihood of co-ordination).

3. CONGLOMERATE MERGERS

Conglomerate mergers - non-coordinated effects

- 3.1 *Paragraph 97:* The second sentence should either say pure bundling is "impossible", not just very unlikely (if products are not bought simultaneously OR by the same customers, as the draft now reads).
- 3.2 *Paragraph 98:* In our view, the starting point of the draft is too timid. If the new entity has "no market power in any of the markets concerned", foreclosure is not just "unlikely", it is inconceivable. We therefore believe that the guidance should state that "foreclosure is unlikely if the new entity does not have a dominant position in at least one of the markets concerned". We also consider that the phrase "is viewed by many customers as particularly important" should be replaced with "is dominant" to make the test clearer.
- 3.3 *Paragraph 99:* The draft Notice should acknowledge that the simultaneous purchase of products is a key factor. After all, although there may be common customers for individual products, the purchase contracts may be negotiated individually.

Conglomerate mergers - coordinated effects

- 3.4 *Paragraph 117-119:* Again, although the Commission cross-refers to the section in the Notice on Horizontal Mergers which covers coordinated effects, the guidance in the draft Notice is very brief. For example, the Notice does not explain why foreclosure from a conglomerate merger will lead to higher prices being enjoyed through coordination. Even on the assumption that higher prices could be enjoyed by foreclosed rivals², it seems to us that this is an example of non-coordinated effects resulting from the lowering of competitive pressure on the non-merging companies. Finally, as regards paragraph 119, multi-market competition could also be said to undermine coordination since competition in respect of many (heterogeneous) products would render coordination more difficult. Overall, we think that the draft Notice should clarify that coordinated effects are very unlikely to arise from conglomerate mergers rather than provide such brief guidance on the issues.

**Baker & McKenzie
(GM/LMA)
April 2007**

² This seems unlikely and is not envisaged in paragraphs 109-116 of the draft Notice, which instead envisages a loss of sales opportunities for foreclosed rivals.